

Message Text

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C O N F I D E N T I A L STATE 067656

EXDIS FOR FRANK MARESCA ONLY

FOLLOWING REPEAT LIMA 2247 ACTIO NSECSTATE MAR 14

QUOTE C O N F I D E N T I A L LIMA 2247

EXDIS

E.O. 11652: GDS
TAGS: EFIN, PE
SUBJECT: NEXT STEPS BETWEEN THE GOP AND IMF

1. SUMMARY: THE GOP HAS REVISED ITS STRATEGY FOR DEALING WITH THE MF AND IS NOW TRYING TO WORK OUT INTERPRETATIONS OF THE STANBDY AGREEMENT AND/OR ADDITIONAL MEASURES SO AS TO BE ELIGIBLE FOR THE SECOND TRANCHE DRAWING BY LATE APRIL EARLY MAY, THUS OPENING THE WAY FOR PRIVATE BANK LOAN SHORTLY THEREAFTER, USG DOES NO APPEAR TO HAVE A DIRECT ROLE AT THIS POINT, BUT WE SHOULD TRY TO MAINTAIN A CALM ATMOSPHERE TO GIVE MAXIMUM OPPORTUNITY FOR THE GOP AND THE FUND TO WORK OUT THEIR DIFFERENCES QUIETLY.
END SUMMARY.

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2. THE GOP IS TIGHT-LIPPED ABOUT ITS STRATEGY FOR DEALING WITH PROBLEMS THE IMF HAS RAISED IN MEETING STANDBY TARGETS, AND THE GENRAL VIEW IN PRIVATE CIRCLES HERE IS THAT THE GOP IS IN A STATE OF INDECISION AND DRIFT. HOWEVER, WE HAVE BEEN TOLD IN STRICT CONFIDENCE THAT THE SITUTATION IS AS FOLLOWS:

3. THERE ARE THREE POINTS OF DIFFERENCE WITH THE FUND, WHICH THE GOP CONSIDERS MATTERS OF INTERPRETATION OF THE STANDBY AGREEMENT:

A) RESERVE LEVEL TARGETS. THIS IS A LARGELY TECHNICAL ISSUE OF HOW CERTAIN FINANCIAL BALANCES ARE TREATED IN THE CALCULATION OF RESERVE LEVELS.

B) NET BORROWING REQUIREMENT OF PUBLIC SECTOR. THERE WAS A DIFFERENCE OF INTERPRETATION AS TO WHETHER THE ROLLOVER OF THE EIGHT BILLION SOLES VOVLET PAYMENT IN JANUARY COULD PERMIT ADDITIONAL FISCAL DEFICIT ELSEWHERE BY THE GOP. APPARENTLY THE GOP HAS ACCEPTED THE IMF VIEW THAT NO SUCH ADDITIONAL CREDIT IS PERMITTED UNDER THE FUND AGREEMENT, AND MEASURES ARE BEING DEVELOPED WITHIN THE GOP TO ADJUST FOR THIS.

C) EXCHANGE RATE. WHILE THE IMF ACCORD PROVIDES FOR A FLOATING RATE, THE GOP INTERPRETS THIS PROVISION TO PERMIT TEMPORARY PERIODS OF STABILIZATION OF THE RATE, WHICH WOULD INCLUDE THE CURRENT ARRANGEMENT AMONG BANKS TO HOLD THE OFFICIAL RATE AT 130. THE GOP CONSIDERS THE 130 RATE A REASONABLE EQUILIBRIUM LEVEL IF CERTAIN SHORT TERM FACTORS, SUCH AS BUNCHING OF IMPORT PAYMENTS AND SPECULATION, CAN BE REVERSED. THE FUND PRESUMABLY WANTS AT RENEWED FLOAT.

4. THE GOP HAS BEEN WORKING WITH THE FUND (INCLUDING THE CONFIDENTIAL VISIT LAST WEEK BY FUND DIRECTOR KAFKA)
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TO REACH AGREEMENT ON HOW TO DEAL WITH THESE DIFFERENCES IN INTERPRETATION. THIS WOULD PRESUMABLY INCLUDE A SCHEDULE FOR ADDITIONAL FISCAL MEASURES BY THE GOP AND AN UNDERSTANDING ON HOW THE EXCHANGE RATE PROVISION WILL BE IMPLEMENTED IF THE 130 RATE CONTINUES TO BE AT SUBSTANTIAL VARIANCE WITH THE HIGHER DOLLAR CERTIFICATE RATE. ACCORDING TO THE GOP, IT WILL TAKE A MONTH OR MORE TO IMPLEMENT SUCH AN UNDERSTANDING, WHICH WOULD PERMIT THE GOP TO OBTAIN THE SECOND TRANCHE OF ITS STANDBY BY THE END OF APRIL EARLY MAY. THE \$260 MILLION PRIVATE BANK PACKAGE COULD BE CONCLUDED SHORTLY THEREAFTER. IN ADDITION, A BRIDGE LOAN WOULD HAVE TO BE ARRANGED VERY QUICKLY WITH SOME PRIVATE BANKS TO COVER THE PERIOD FROM NOW UNTIL MAY. THE BRIDGE LOAN MIGHT BE OBTAINED ON THE BASIS OF AN AGREED SCHEDULE BETWEEN THE GOP AND THE FUND FOR BRINGING THE GOP INTO COMPLIANCE.

5. COMMENT: THIS TIMETABLE FOR THE SECOND TRANCHE/PRIVATE BANK LOAN IS CONSIDERABLY EXTENDED FROM WHAT WAS ANTICIPATED ONLY A WEEK OR TWO AGO, AND EVIDENTLY REFLECTS MORE SERIOUS PROBLEMS ENCOUNTERED WITH THE FUND. THE GOP VOICES OPTIMISM THAT THE REVISED SCHEDULE IS WELL

ON TRACK, BUT THIS MAY MERELY REFLECT THE PERENNIAL OPTIMISM OF THE GOP IN DIFFICULT SITUATIONS. HOWEVER, THE UNSUAL DEGREE OF SECRECY THAT PREVAILS BOTH HERE AND BY THE IMF IN WASHINGTON COULD INDICATE THAT THERE IS INDEED A SERIOUS ATTEMPT UNDERWAY TO RESOLVE THESE PROBLEMS. THE FIRST CLEAR INDICATION OF THE OUTCOME MAY BE WHEN THE GOP SEEKS TO NAIL DOWN A BRIDGE LOAN. PRESUMABLY LINED TO AN UNDERSTANDING WITH THE FUND THAT MEASURES WILL BE TAKEN TO MAKE THE GOP ELIBIBLE FOR THE SECOND IMF TRANCHE BY THE END OF APRIL/EARLY MAY. WE DON'T KNOWN HOW CLOSE THE GOP IS TO A LIQUIDITY CRUNCH, BUT THERE IS MUCH TALK OF SCRAPING THE BOTTOM OF THE BARREL.

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6. THE GOP IS OBVIOUSLY IN A DELICATE POLITICAL SITUATION, PARTICULARLY IF ADDITIONAL UNPOPULAR FISCAL MEASURES AND EXCHANGE RATE ADJUSTMENT ARE IN THE OFFERING. THERE IS A VIEW IN PRIVATE CIRCULES THAT THE GOP SHOULD CHANGEITS ECONOMIC TEAM AND RENEGOTIATE THE IMF ACCORD. THIS MAY YET BE THE FINAL RESULT, PARTICULARLY IF BUDGET LEVELS BECOME A BIGGER PROBLEM THAN THE GOP IS NOW WILLING TO ADMIT.

7. WE HAVE NO APPARENT DIRECT ROLE TO PLAY AT THIS POINT, BUT WE WHOULD TRY TO MAINTAIN A CALM ATMOSPHERE AND THUS GIVE MAXIMUM OPPORTUNITY FOR THE GOP AND THE FUND TO TRY TO WORK OUT THEIR DIFFERENCES QUIETLY. THE ISSUE OFNATIONAL SOVEREIGNTY AND PURPORTEDLY UNWARRANTED INTER-FERENCE BY THE FUND IN INTERNAL PERUVIAN AFFAIRS IS A CONTINUING PROBLEM FOR PRESIDENT MORALES BERMUDEZ, BOTH FROM WITHIN HIS GOVERNMENT AND FROM OUTSIDE CRITICS. IF A COMPROMISE RESOLUTION OF THE BUDGET ANE EXCHANGE RATE ISSUES CAN BE WORKED OUT BEHIND THE SCENES WITHOUT APPEARING AS THOUGH THE GOP HAS CAPITULATED FULLY TO THE FUND, IT WOULD IMPROVE THE POLITICAL CHANCES FOR EFFECTIVE IMPLENENTATION.
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